ChantreyVellacottDFK

Agriculture & Estates Briefing

Russian Edition 07

Introduction

Whilst the UK Farming scene has recently been dominated by a buoyant arable sector, a depressed livestock sector and promises by retailers to increase prices, I was fortunate to be invited to visit two working Russian farms in September this year. British nationals beneficially own both farms. Consequently, this newsletter reflects my impressions of the farming of that unique country and the opportunities it currently offers.

Geography

The USSR was once the biggest state in the world and at its height covered 8,603,852 square miles (Great World Atlas 1967). The United Kingdom covers 94,207. In other words it is over 90 times the area of the UK. There are 640 acres in a square mile.

Of that massive area, even in Soviet times, less than 10% was under cultivation.

History

The history of the USSR is relatively well known. 1917 saw the Communist revolution, 1941-45 the Great Patriotic War and eventually the system failed in 1989.

Some of the countries formerly comprising the USSR have gained independence, others have remained as satellites of members of the Russian Federation.

Last week Russia was described to me as a 'Police state trying its hardest to act democratically'.

The Implications

When Communism was at its height many collective farms were established, effectively nationalising the agricultural holdings of the previous czarist farmers. Whilst perhaps never particularly efficient in western terms, they provided a rural control structure for the Kremlin and potentially productive units based on large fields, typically more than 100 hectares.

When in 1989 the system crashed the central money was turned off and the collective farms simply fell into dereliction. Farm staff were not paid and so reverted to a subsistence basis of living, based on a system similar to the medieval 'strip system' in England. Without being disrespectful in any way the rural housing was (and is) in many ways third world. The villagers produced what they ate, whilst the large fields or 'massifs', did nothing but grow weeds. 'Massifs' next to forests or woods became, or started to become forestated.

The infrastructure started to fail. The railways always play an important part in large countries such as Russia and grain was historically taken to the railheads and distributed either internally or taken to ports for export. Again, when the money ran out the storage units at the railway fell into disrepair and wet corn was either left to rot or was fed to the birds. There appear to be many birds; everyone appears to keep geese.

No new equipment was purchased as there was no money to pay for it. The farms we visited resembled a collectors yard of 1970 Soviet memorabilia. Looked over by the mandatory statue of Lenin a heady mix of Belarus tractors and 3 furrow ploughs stood in the machine yard, obviously not capable of attacking the 25,000 acres that previously were under cultivation. Consequently, last year (2006/07) less than 2,000 of those 25,000 acres were actually under the plough.

The Opportunity

The opportunity is to earn money by rejuvenating the Russian countryside by injecting Western cash, equipment and expertise. It is my belief that an enhanced income can be achieved if done properly and professionally.

The soil is terrific. The Area that we visited boasted the 'black earth', quite capable of growing wheat, barley potatoes and maize. Oil seed rape is currently under trial, testing its ability to withstand the Russian winter which creates a 'winter kill percentage' each year. Yields of 2 – 2.5 tons of wheat per acre are quite achievable, with minimal inputs.

The labour force, once weaned from vodka is also available. A weekly wage of 1000 roubles (£20) is the norm. There is an abundance of labour, however, some more willing than others.

There is an infrastructure and a means of sale. Units close to railheads are obviously the most attractive. What is not attractive is the current practice of carting the corn in 5 ton petrol trucks to the railhead! Its eventual price however compares favourably with UK prices.

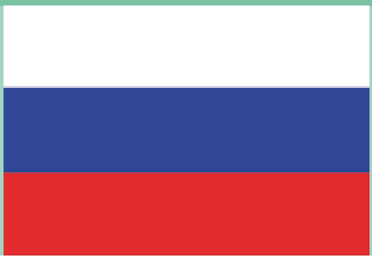
I should also say that at no time did I spot ACCS/ FABBL or DEFRA officials.

The Difficulties

Political climate. Whilst clearly not stable previously, Mr Putin has reintroduced a degree of stability not enjoyed since old communist times. He is also a realist who wishes to safeguard his food supply.

Obtaining the land / language. Russian bureaucracy cuts in here and a Russian national is almost a prerequisite. It is not insurmountable as the political impetus is seemingly to rediscover the Russian powerbase of old.

Weather. Winter and rainfall (or lack of) can have dramatic effects on yields.



The Arithmetic

Just in our short journey we estimate that we must have travelled through at least 1,000,000 uncultivated acres. If each of those acres were to come back into production and produce 2 tons of wheat then the resultant 2million tons would represent nearly 10% of the UK wheat harvest.

The reality is that there is far more than 1,000,000 uncultivated acres and western know how and expertise would, I am sure extract far more.

Why Consider Russia?

Russia is clearly not an easy option, but with application and capital, it does represent a terrific opportunity to conduct large scale arable operations, with the potential for returns far in excess of this country, even with the current higher prices. In some ways it should be considered 'frontier country' but the risk versus reward equation certainly warrants serious consideration.

FAQ: What do you buy?

Non Russians effectively buy 49 year leases, backed up by land certificates.

FAQ: What if the Russians kick out the Foreigners?

Russia does have that reputation (BP in Sakalin etc) but when taking that step they have traditionally compensated the outgoing tenant.

FAQ: What about the Mafia?

The Mafia are apparently more active in the cities and are apparently in decline due to Mr Putins 'control mechanisms'.

What Gross margin can be produced?

I think a margin of £150 per acre should be achievable for wheat. On the 25,000 acres I visited this gives a total annual margin of £3.75million to pay for machinery, men and vodka! I also understand that the land certificates have also started to increase in value, thus giving a potential capital gain.

Conclusions

If you would like to discover more or be put in touch with others currently farming in Russia please let me know. Chantrey Vellacott DFK have a DFK office in both Moscow and St Petersburg and would be keen to help the British Farmer seeking to expand into this fascinating country.

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The Abolition of Agricultural Buildings Allowance

Returning to the United Kingdom, the now Prime Minister Gordon Brown, in his last Budget saw fit to firstly reduce the rates of Agricultural Buildings Allowance and then abolish it in total from 6 April 2010.

The rates in the meantime are to be reduced as follows:

3% pa from 5 April 2008
2% pa from 5 April 2009
1% pa from 5 April 2010
Thereafter 0%.

Therefore, for the first time in living memory, there will be no relief for the construction of agricultural buildings or structures.

Other Capital Allowances

At the same time as the changes mentioned above, the then Chancellor also made changes to the taxation of Long Life Assets and plant and machinery integral to a building. These changes will be the subject of the next newsletter when the final details are ascertained. In any event, they only apply to machinery contained as part of a building and do not apply to the actual construction itself.

Who To Contact

For further information on any item within this briefing or about Chantrey Vellacott DFK please contact John Harris or Richard Clarke at our Northampton office or contact any of the listed contacts at our various offices. Alternatively, visit our website at **www.cvdfk.com/sectors/agriculture**, where further copies of this briefing, along with past issues, may be downloaded.

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Published by Chantrey Vellacott DFK LLP, Russell Square House, 10/12 Russell Square, London WC1B 5LF. Offices in Brighton & Hove, Croydon, Leicester, London, Northampton, Reading, Stevenage and Watford.

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